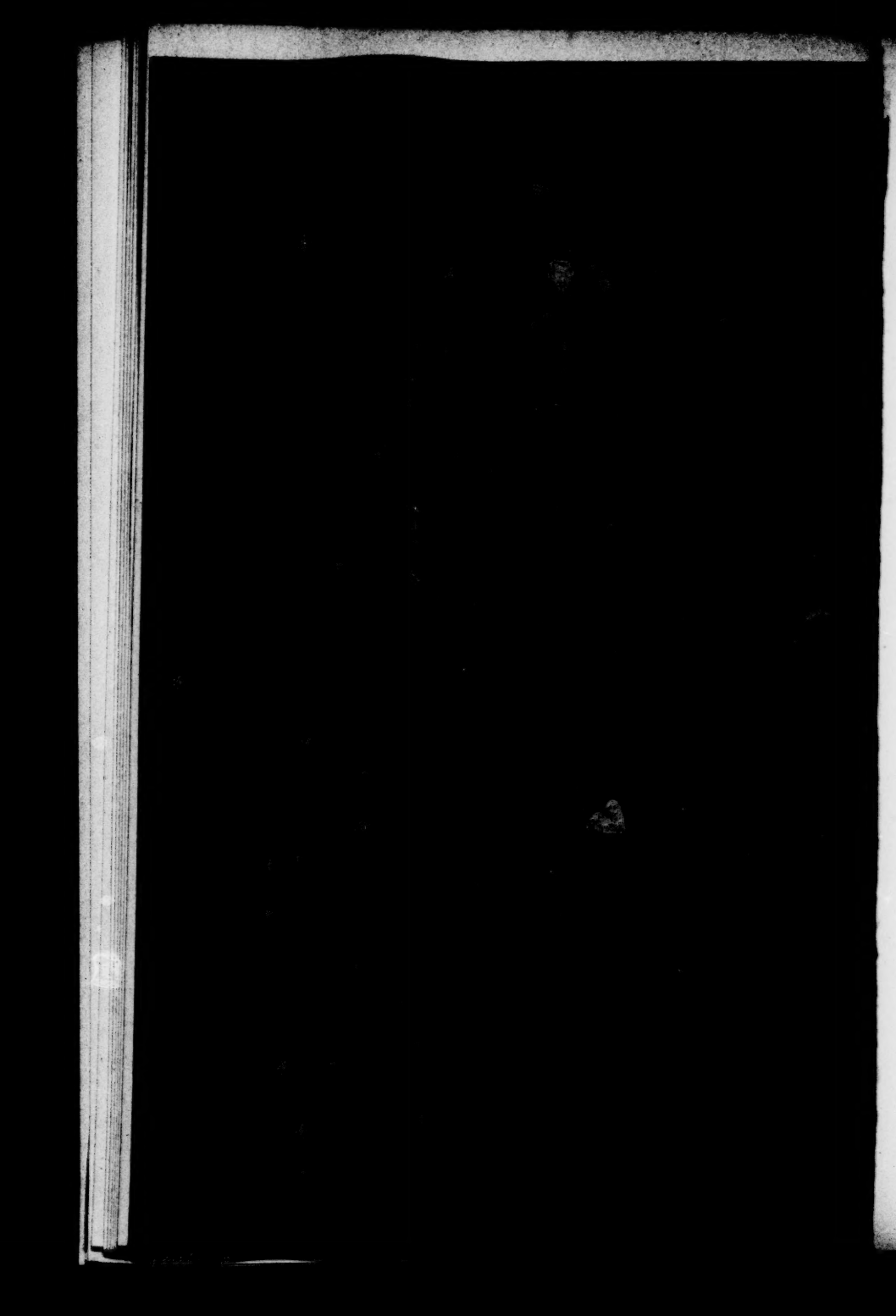

Supreme Court of the United States.

OCTOBER TERM, 1893.

No. 556.

CHARLES MORAN, TRUSTEE, APPELLANT,

versus

THE PITTSBURGH, CINCINNATI AND ST. LOUIS RAILWAY COMPANY, SAMUEL JEANS, THE TRUSTEES OF CADIZ TOWNSHIP, RUMLEY TOWNSHIP, AND GERMAN TOWNSHIP, IN HARRISON COUNTY, OHIO; THE TRUSTEES OF STEUBENVILLE, IN JEFFERSON COUNTY, OHIO, AND THE CITY OF STEUBENVILLE, OHIO.

BILL IN EQUITY ON APPEAL.

BRIEF OF J. M. ESTEP, FOR APPELLEES.

STATEMENT.

The railroad property now known as the Cincinnati and Muskingum Valley railway was originally known as the Cincinnati, Wilmington & Zanesville railroad, the same being owned by a company of that name, which was incorporated in Ohio in the year 1851. On about the 15th day of April, 1852, said last-named railroad company issued seven per

cent. bonds to the amount of $1,300,000 and secured the same by mortgage on the railroad of said company; that by reason of the non-payment of the interest on said bonds a decree was rendered in the United States court for the southern district of Ohio, by virtue of which said property was on the 27th day of August, 1863, sold at public sale to Charles Moran for the sum of $600,000, said sum being the highest amount bid for said property at said public sale.

The purchasers at said sale, represented by Charles Moran as aforesaid, reorganized said property and became incorporated in 1864 as the Cincinnati & Zanesville Railroad Company, one of the terms of said reorganization being that the first-mortgage bonds of said reorganized company should amount to $1,300,000, bearing interest at the rate of seven per cent. per annum.

The said Cincinnati & Zanesville Railroad Company having failed to pay certain interest on said bonds, about the 30th day of April, 1869, judicial proceedings were instituted in the circuit court of the United States for the southern district of Ohio, and such proceedings were had that an order of sale was issued to said Charles Moran, trustee and special master commissioner, in pursuance of which, on the first day of December, 1869, he sold the said railroad property to Thomas L. Jewett for the sum of $1,004,000, that being the highest and best bid.

The purchasers at said sale, represented by said Thomas L. Jewett, reorganized said property and became incorporated as The Cincinnati & Muskingum Valley Railroad Company, one of the defendants in this suit.

See pages 50 and 51 of Defendants' Book of Testimony.

In 1870–'1 the road was extended from Zanesville to its present connection with the Pitts., Cin. & St. L. Railroad Company at Dresden Junction. The bonded indebtedness was then increased to $1,500,000, the extra $200,000 having

been added for the alleged purpose of extending the road to Dresden Junction, and to secure said bonds the mortgage now in suit was executed, dated September 1, 1870.

All of these companies were insolvent and unable to earn and pay the interest on the bonds, except in part, and occasionally under peculiar circumstances, to be hereafter stated.

This fact Charles Moran thoroughly understood, for he was interested in the road from the beginning, in 1851, and had "sad experience" of the results when operated by its own organizations, long before this lease now in controversy was executed.

The Valley road was operated under its own management until May 1, 1873, when the Pan Handle Company took possession under the alleged lease.

For a short time returns are made and interest paid, but the testimony clearly shows that this is done at the expense of the property, by failing to keep or place it in good condition. It was only putting off the evil day. For reasons stated in Mr. Becker's testimony, the property is a very difficult one to keep in order, and needs large improvements and repairs each year in order to operate it with safety.

A great part of the correspondence in Complainant's Book of Testimony between Charles Moran and Colonel Scott principally can have no legal bearing upon these defendants, but it does show clearly the design and object of Charles Moran in the whole business. It shows clearly that he knew his own road would not and could not pay if confined to ITS OWN income.

He, therefore, desired to get up some plan by which the income of the Pan Handle railway could be reached for the purpose of making his bonds good. He and his friends held $748,000 of these bonds, and, as the Pennsylvania Railway Company held the remaining $752,000, he hoped that Thomas A. Scott, the president of the company, would assist him in obtaining such an arrangement. As Thomas A. Scott, representing the Pennsylvania Railway Company,

But, of course, this would not satisfy Moran. He had too much experience as to the "unhappy" results of the road when they had heretofore obtained "every dollar out of the revenue received from its business."

Your company, Mr. Scott, has a large interest in these bonds. You can control the Pan Handle Company. Our own road will not pay; that we both well know. You can have the bonds guaranteed or, at least by virtue of your power, you can divert traffic from the Pan Handle and thus make our bonds good. That is his idea.

But Mr. Scott would not agree to this. He would not agree to build up these bonds at the expense of the Pan Handle at that time, but he was willing that the Valley road should have the entire results of its own trade and traffic.

In page 80 of the Record Col. Scott writes Moran under date November 19, 1872:

"Of course our company would not be willing to assume the responsibility you name in your letter, but they are willing to work the line at its cost and give the stockholders all the net results. This is all, I think, you in justice can ask them to do."

Moran knew this was all he had a right to ask, but he still insists and hopes that Scott may yield. Finally, Scott lets him know that he will not divert trade or traffic from the Pan Handle for any such purpose, and if the matter cannot be arranged without entering into such a scheme as that the whole matter might drop, and the road continue under the old management as heretofore.

Then Moran thinks best to yield the point, and he writes to his friend Churchill under date Dec. 28, 1872, in Record, page 99, and among other things says: "Mr. Scott assures me that the sincere desire of P., C. & St. L. Co. is to develop the traffic of our road, and that they will do everything in their power to do so, except that for the time being THEY

CANNOT TRANSFER ANY OF THE THROUGH TRAFFIC FROM THEIR ROAD TO OURS. But this we can hardly expect them to do, and they will no more do it under present circumstances than after the execution of the lease, so that, by assenting to this lease, we are no worse off in this respect, whilst we obtain, on fair terms, the requisite means to develop our local traffic, which, in time, must enable the company to declare some dividends on the shares."

Of course he knew that he had no right to expect that the through traffic of the Pan Handle road should be diverted to his road. He knew that was wrong, but he hoped that Col. Scott, having so much business on hands—so many irons in the fire—might overlook the injustice of it and hastily and inadvertently assent to it.

He fully understood the wrongful means that must be resorted to in order to put the scheme in operation. He saw the point in the power of the large majority of stock held by the Pennsylvania Railway Co. in both the lessor and lessee companies. He knew and understood that in fact they were making a lease of their own road "to themselves." And he proposed to take advantage of this fact, if he should ever find it necessary to appeal to the courts.

See Record, page 106. Moran's private letter to Churchill of date Jan. 6, 1873, in which he says: "When we apply for redress to the courts, the very fact that the majority made a lease of the road to themselves will be of great assistance to us."

But he was, notwithstanding, desirous to have "that majority" divert traffic to his road.

He also knew that the scheme or plan for accomplishing such a purpose had best be kept secret.

That it would not be prudent to expose to the minority stockholders of the Pan Handle Company or to the public the means resorted to to bring about this clause in the lease for the "advance" from the funds of the Pan Handle Company to pay the debts of the Valley Company.

He also knew that any "advances" or loans that might be made could never be repaid or refunded out of the honest proceeds or income of his own road, and that is the reason he so strenuously insisted on the clause in the lease that such "advances" "should be returned out of the subsequent earnings, AND NOT OTHERWISE."

In 1877 he desires to have a further assurance deed executed, and because it was refused he thought proper to make a threat of suit and of EXPOSING this correspondence in order to accomplish his purpose.

In his letter of April 21, 1877, Record, page 125, he says: "If your company refuses to give it, I shall be forced to apply to the court for its execution, which I shall greatly regret, as it will give trouble and expense to both parties AND GIVE PUBLICITY TO THAT WHICH HAD BETTER BE KEPT BETWEEN THE PARTIES."

The Valley Company was calculated for local traffic, but not for a through line. The Pan Handle route, by way of Columbus from Dresden Junction to Morrow, is 139 miles. From Dresden Junction, by the Valley road, to Morrow is 148 miles.

The testimony of M. J. Becker, on pages 3 and 4 of Defendants' Book of Testimony, shows that there are 55 bridges on the Valley road, besides a great number of smaller openings for water-ways, and that by reason of floods and other accidents the cost of maintenance is "unusually expensive."

That at the time of the lease the road was in a very bad condition, and the lessee company soon placed it in good condition, and that it now, or when it was surrendered back, to wit, January 1, 1886, is in a much better condition than when the lease was executed.

The testimony of Mr. Renner, on pages 11 and 12, shows that the expenditures by the lessee company for betterments and improvements were $140,969.00, which improvements the lessor company agreed to make, but failed and neglected to do so.

The testimony further shows that the road was fairly and honestly managed and operated, accounts properly kept, and every dollar of its own revenue appropriated to its own use.

No traffic was ever diverted FROM it in any shape or form.

The complaint of the complainant is that traffic was not diverted FROM the Pan Handle.

That the power existed to wreck the Pan Handle is not denied. But the strange thing is that it should be insisted that it ought to have been exercised.

Judge Hoadly admits, on pages 12 and 13 of his brief, that "The experiment of this lease, inaugurated under these favorable circumstances, has proved a financial failure." And, then, he adopts Moran's complaint, overlooking the rights of the Pan Handle Company to its own traffic, and states the alleged cause of the failure thus: "This, however, is not the fault of the lessor, but of the lessee company, which, as it controlled both lines, could easily have placed business enough upon the Mus. Val. line to avoid this consequence. Its entire through business, both freight and passenger, has been done on the line through Columbus, instead of over the Mus. Val. Co."

But this is the very thing that Moran said to Churchill that Scott would not agree to do, and that they had no right to expect.

This correspondence clearly shows that Col. Scott did not and would not agree to take traffic from the Pan Handle in order to build up the Valley Company and make the bonds good. Each road was to have and retain its own traffic—the entire proceeds of its own business. Anything else, he said, would be "unjust," and Moran had no right to ask more.

In no event was the Pan Handle Company to have any profit or any part or the income of the Valley road.

Thus far Scott held out for the right. But Moran was

still persistent. He presented the idea, time and again, that the Penn. R'y Co.'s $752,000 bonds would be worthless unless something was done to provide for the interest, and Scott finally agreed that the clause for the "advance" should go in the lease, and thus the fraud and wrong upon the minority stockholders in the Pan Handle Company was accomplished.

Moran, having thus succeeded in having this unjust clause placed in the contract, cannot, at this day, claim to have been deceived in any way.

His claim for himself and friends is the same old claim, substantially, which he has held for over thirty years.

He invested nothing and gave nothing on the faith of this lease, and has no equities whatever. He is in no better position than the lessor; and, calling upon a court of equity to further enforce this iniquity, he must clearly show his right and the contract under which he claims it.

As it is conceded that this "advance," already made to the extent of over $1,000,000, can never be returned or repaid, there is no equity or justice in allowing the funds of the Pan Handle Company to be further squandered in paying the old debts of the Valley Company.

It may be well enough to state, also, that the record, page 31 of Complainant's Book, shows that Mr. Moran had knowledge of the suit of Samuel Jeans *et al.* at Steubenville, as early as June 30, 1885; that he was requested to take part in the defence of that suit, brought to set aside the said lease, and he refused.

The decree was rendered in said suit setting aside the lease on the 24th of Nov., 1885.

The bill in the present case was filed by Moran September 9, 1885.

On page 57 of Defendants' Book of Testimony it is shown that the minute books of the directors and stockholders of the Valley Company contain no reference whatever to any action by J. Edgar Thompson and Charles Moran, trustees,

or either of them, adopting or confirming the said lease, nor of any action of the stockholders or directors of said Valley Company assigning said lease to said trustees, or in any manner placing the same under the mortgage previously executed.

On pages 37 and 38 of Judge Hoadly's brief will be found the decree asked by complainant Moran, trustee of the mortgage. He prays "that it may be held and established, notwithstanding said collusive suit and anything done therein, that the said lease and contract in equity belong and appertain to the holders of said mortgage bonds, and to plaintiff, as their trustee, as a muniment and part of their title, and that said lease and contract are valid; and that said holders and this complainant are entitled to enforce the same, and to collect said rents as security for said bonds; and that all the estate and reversion of the lessor in said railway property, with the benefit of the lease aforesaid, and the right to receive the rents accruing upon said lease, and to enforce the performance of its covenants, may be sold and disposed of by a master commissioner, to be appointed by this court, but without dispossessing the lessee company of its possession or any of its rights under said lease, and for such other and further relief as the complainant may prove to be entitled to."

ARGUMENT.

We think it very clear that Moran is not entitled to any such decree as prayed for.

He is entitled to foreclose his mortgage and sell the mortgaged property, and that puts an end to the lease. The purchaser will take the property described in the mortgage and nothing else. As the lease is subsequent to the mortgage, it in no way bound or affected the mortgagee. As the mortgagee was not and never became a party to the lease, he is in no way bound by any of the covenants in the lease.

If the mortgagee obtained any rights to this lease he obtained them on the day of its execution and became also bound by its covenants. It will not be seriously claimed that the lessee, under the circumstances shown in this case, could have compelled Moran, the mortgagee, to have performed the covenants in this lease, which were by its terms to be performed by the lessor. The lease is in writing and must be construed by its terms, and binds the parties thereto, and none other.

No contract is shown of assignment, adoption, or ratification, and Moran could not adopt it or become bound by it merely by the secret operations or intentions of his own mind. He never did intend to be bound by it. The idea of mutuality of covenants never entered into his mind.

These principles are elementary and do not need the citation of authorities.

The mortgagee is in no better condition, at any rate, than the lessor, and, as the lessor is in default and refuses to perform the covenants on its part, a court of equity will not specifically enforce the covenants on the part of the lessee.

Judge Hoadly claims that he is entitled to the relief prayed for mainly upon two grounds:

1. That this lease is "after-acquired property" and thus covered by the mortgage.

2. That the clause for an advance of the funds needful to meet the coupons is really a promise upon consideration to pay the debt of the lessor to the mortgagee.

Neither of these claims can be supported by reason or authority.

The clause for the "advance" is really and in substance a clause for a loan to be returned and repaid in a certain way if there shall be a fund for its repayment. It is surely not evidence of a debt. The mortgage debt of the lessor does not become the debt of the lessee because he promises to advance or loan the lessor money. It may have been for the interest of both lessor and lessee that no default should be

made under the mortgage, and hoping that the road, when put in good order and in full operation under the contract, would be able to meet its own obligations, it may not have been considered unfair or unjust to the Pan Handle to make this "advance" for a short time if it was honestly intended to be returned or repaid. But it surely did not become the debt of the lessee simply because he promised to advance or loan the lessor money with which to pay it.

Neither can the promise for the "advance" be considered "rent." No rent, as rent, was to be paid. The lessor was to have the entire income after expenses. Besides, rent is a debt owing for the use of property, and of course when paid it is not to be returned or paid back.

Of course, if the plaintiff has no interest in this lease that is an end of the matter so far as these defendants are concerned.

Judge Harrison has fully and elaborately discussed the proposition, maintaining that "the plaintiff never acquired a lien upon nor an interest in the lease set forth in the pleadings," and that therefore he has no right to the decree prayed for.

This he has so clearly demonstrated that I will have but little to say on that question, but intimately connected with it are other points and conclusions which I shall briefly beg leave to call to the attention of the Court.

I.

We claim that the decree in Jefferson county, O., November, 1885, in the case of Samuel Jeans *et al. v.* P., C. & St. L. R'y *et al.*, setting aside said lease, is conclusive and binding as to the invalidity of the lease.

For the record of that decree see page 37 of the Gray Book.

As Moran was not a party to the lease and had no legal interest in it, we claim that he was not "a necessary party" to the said suit of Samuel Jeans *et al.*, and that the decree

in that case annulling the lease between the proper parties is binding and conclusive.

That he had no legal interest in the lease we think quite clear.

His mortgage was executed two years before the lease. He did not sign it or in any way, then or afterwards, become bound by its terms. He could not adopt or ratify it merely in his own mind.

He could only get an interest in it by some valid agreement. There was no such agreement. If there are obligations they must be mutual. He could at any moment, on default, foreclose his mortgage or take possession of the road.

He could not adopt a part and not the whole.

There is, of course, a very material difference between the rights of a mortgagee in the cases of a prior lease and a lease subsequent to the mortgage.

Moran, of course, would naturally desire his mortgagor or debtor to make good contracts and do well, so as to be able to pay the interest; but surely this very natural desire gave him no legal interest in the lease itself.

Even if the clause for the "advance" of the interest to meet the coupons had not been, as it is, a loan, but a fixed sum, as rent to be paid the lessor for the use of the road, Moran, as mortgagee, in the case of a subsequent lease would have no lien on or control of the lease or the rents.

The disposition and control of the rents in such case would rest entirely with the mortgagor; and, notwithstanding the mortgage, the rents would be liable to attachment by the lessor's creditors.

It is certainly well-settled law that until the mortgagee takes possession of the property or a receiver is appointed by proper action in the courts the mortgagor has the entire control of the property, the rents, and profits.

In 1 Jones on Mortgages, sec. 777, it is laid down that where a lease is executed subsequent to the mortgage

"there is no privity of contract between the mortgagee and lessee, and until actual entry by the mortgagee, or the lessee expressly promises to pay rent to him, he can maintain no action against the lessee to recover it." (See also sec. 670.)

And in the very late and well-considered case of Teal *v.* Walker, 111 U. S., 242, it is said: "Where the lease is subsequent to the mortgage it is well settled in this country that, as no reversion vests in the mortgagee and no privity of estate or contract is created between him and the lessee, he cannot proceed, either by distress or action, for the recovery of the rent, * * * and even upon condition broken, if he wishes to receive the rents, he must take means to obtain possession. * * * the mortgagor contracts to pay interest, not rents."

The Court further says (citing from 4th Kent's Com., 157): "The mortgagor has a right to lease, sell, and in every respect to deal with the mortgaged premises as owner so long as he is permitted to remain in possession and so long as it is understood that every person taking under him takes subject to the rights of the mortgagee, unimpaired and unaffected."

The mortgage has thus no binding claim, interest, or lien on the lease or the rents accruing under it by virtue of his mortgage; and there is no clause in this mortgage professing to give him any such right or claim.

But even if the attempt had been made in this mortgage in express terms to cover the income, rents, and profits of the lease it would not have changed the general rule as above stated.

This point is clearly settled in the case of Gilman *v.* Telegraph Co., 91 U. S., 603. The opinion is delivered by Justice Swayne. "Until possession is taken or a receiver appointed the mortgage does not transfer the 'income' to the mortgagee, although the 'income' is mentioned in the mortgage. Until possession taken the whole income belonged to

the railroad company, and was liable to the creditors of the company the same as if the mortgage did not exist."

The same doctrine is distinctly held in The American Bridge Co. *v.* Heidebach & Courtright, trustees. 4 Otto, U. S., 798. Opinion by Judge Swayne.

"Where a mortgage upon a bridge executed by bridge company includes the rents, issues, and profits of the bridge until the mortgagee take possession of the property, such rents, issues, and profits belong to the mortgagor, and until that is done they are liable to the claims of the creditors of the mortgagor in preference to the mortgagee."

It is clear, we think, there is nothing in this mortgage, either by express terms or implication, that gives Moran, as mortgagee or trustee, any legal interest in this alleged lease. The lease is not mortgaged.

In 1 Jones on Mortgages, section 776, it is laid down that "A mortgagor cannot make a lease of the mortgaged premises that will be binding upon the mortgagee. Upon a breach of the condition the mortgagee may enter and treat the lessee as a tresspassor, and without notice bring ejectment." And in section 772, "A mortgagee has no specific lien upon the rents and profits of the mortgaged land, unless he has, in the mortgage, stipulated for a specific pledge of them as part of his security. He has no claim upon them until he has the right to take possession of the premises under his mortgage." And section 667, "The commencement of an action against him by the mortgagee to recover possession does not change his rights in this respect, and he is not accountable for the rents and profits accruing afterwards and before the mortgagee is entitled to possession under the judgment. If the mortgagee wishes to receive the rents and profits he must take early means to obtain possession."

Of course the tenant may agree to pay rent to the mortgagee after he obtains possession, "but this is a new under-

taking, and must be valid as a new agreement if valid at all." Section 778.

It will be observed that by this mortgage now in suit there is no specific pledge of the income or rents.

The clause in the mortgage permitting the Valley Company to remain in possession until default does not, as claimed by Judge Hoadly, "give the ownership of the accruing income to the company." That clause is simply a statement of what the law would be without it. The mortgagor has the right to the premises and use of the property under the general law, not simply "until the moment of Moran's demand or of the filing of his bill," but until the mortgagee actually takes possession or is entitled to possession "under the judgment," or until a receiver is appointed and takes possession. In the meantime he needs no "permission" to take and use the rents or profits.

Upon default, then, the mortgagee does not take possession of the lease or the rents accruing under the lease, but he takes possession of the property, and thereby obtains full control of all its profits and income in spite of the lease or any other contract made by the mortgagor after the execution of the mortgage. By taking legal possession he gets the use of the property, and he may control it personally or through his agents and employees, and thus get the income and profits and rents if he sees fit to rent it himself.

THE LESSEE DID NOT ASSUME THE MORTGAGE.

It is claimed, however, that Moran was instrumental in having the following clause inserted in the lease, and that by virtue of said clause he in some way is brought in privity with the lease, and in some way obtains control of the lease or of the funds to be "advanced" to the lessor in a certain event. That clause is as follows:

"Provided, however, that in the event of the net earnings of the line of road hereby demised not being sufficient to

protect the interest of the existing first-mortgage bonds of the party of the first part, as it matures, the party of the second part shall advance the needful amount to pay the coupons at maturity, and charge such advance, over net earnings, in open account to be returned out of subsequent earnings and not otherwise."

Surely this clause creates no liability by the lessee company to Moran, the mortgagee. There is no privity of contract here between the lessee and Moran. There is no assumption of the debt of the mortgagor.

If the advance or loan is made to the lessor Moran would desire and expect that the interest would thus be paid; but his mortgage gives him no legal claim upon it. The lessor might appropriate the money to other claims or debts. The contract is with the lessor and not Moran.

It is true, there are a class of cases where a promise, on a sufficient consideration, is made to A for the benefit of B, where it is held that B may enforce the contract and promise, as in Lawrence *v.* Fox, 20 N. Y., 268.

Brewer *v.* Maurer, 38 O. S., 550.
Emmett *v.* Brophy, 42 O. S., 82.
1 Jones on Mortgages, section 755, *et seq.*

But these decisions cannot avail Moran in this case. He is no party to the contract or promise to "advance." There is no promise to pay him.

And all the cases agree that, where property subject to a mortgage is leased or sold, in order to give this right, there must be, 1st, an express promise by the vendee or lessee to pay the mortgage debt, and, 2d, this promise must be upon a valuable consideration.

The amount to be paid must, by the arrangement, become THE DEBT OF THE LESSEE.

In most cases the property is sold for a certain price, and the purchaser who assumes the payment retains enough of the purchase-money to pay the mortgage debt. It is none

of his business whether the debt to the mortgagee is great or small, just or unjust. The vendor has given him the money with which to pay it.

This idea of the obligation to pay thus becoming the debt of the lessee or vendee is absolutely the controlling factor.

Of course, the doctrine cannot apply to a case where nothing is received with which to pay the mortgage. When the entire net income of the property, as in this case, is to be turned over to the lessor, and if the mortgage is to be paid through the lessee, it must be by a loan or advance, not because it has become the debt of the lessee.

By all the authorities, where the purchaser agrees to pay the incumbrance out of the purchase-money he becomes the principal debtor, and in equity he holds the money in trust for the mortgagee. It thus becomes the debt of the vendee.

This matter is made very plain by the late case of Shepherd *v.* May, 115 U. S., 505–512.

In the syllabus it is laid down: "In the absence of the mutual agreement of the grantor, grantee, and holder of the incumbrance to that effect, the relation of principal and surety does not exist between the grantee or grantor."

And this agreement to pay must be express. It cannot be inferred from a statement of the vendee that he had the incumbrance to pay. Same case.

Nor from the fact that he had made several payments of interest to the mortgagee, for he may have done that simply to avoid a foreclosure.

Elliott *v.* Sackett, 108 U. S., 132, 143.

But here there is no agreement to pay the mortgage or its interest or any part of it.

A promise to advance or loan money to a mortgagor with which to pay a mortgage is a very different thing from a promise to pay the mortgage itself.

The authorities for this are clear and decisive. See 1 Jones

on Mortgages, 3d edition, sec. 755 to 770, for a full discussion and a fair brief on the question.

Garnsey *v.* Rogers, 47 N. Y., 233, 239.
Merrill *v.* Green, 55 N. Y., 270.
Second National Bank *v.* Grand Lodge, 98 U. S., 123.
Pardee *v.* Teat, 82 N. Y., 389.

This last case is a very complete one and should be examined. The circumstances, as there shown, must be such as to cause the mortgage assumed to become justly and in equity the debt of the vendee and not in form merely.

If the mortgage gives Moran in terms no legal interest in this lease and this promise "to advance" money by the lessee to the lessor for the purpose of paying interest on the mortgage is not a contract with Moran or a debt of the lessee which Moran could enforce, this should end the matter.

Surely there has been no new CONTRACT or arrangement since the execution of the lease whereby the lessee has bound himself to Moran. The mortgage and lease are in writing and speak for themselves.

Surely the fact that Moran received the money thus wrongfully "advanced" for several years or the manner of its advance or payment or his NOW SAYING that he "adopts" and ratifies the lease cannot help him. There is no particle of evidence showing that Moran, as mortgagee, ever became a party to this contract, or that he ever consented to be bound by the covenants of said lease or contract in any way. If there are to be binding obligations or covenants they must be mutually binding on both or neither is bound.

At any moment, if default be made by the mortgagor, Moran could have foreclosed his mortgage without any regard to the lessee whatever.

Surely the fact that he secretly worked with T. A. Scott

to get this clause for the "advance" into the lease makes him no party to the lease nor binds him to its terms.

The parties to this lease are, then, alone the lessor and lessee—the Valley Company and the Pan Handle Company. They made it, put it in shape, and executed it, and they can unmake it or rescind it.

1 Jones on Mortgages, sec. 763.
Trimble *v.* Strotter, 25 O. S., 378.
Brewer *v.* Maurer, 38 O. S., 550.
Emmett *v.* Brophy, 42 O. S., 89.

The "after-acquired" property clause in the mortgage does not help the matter.

Clearly, taken in connection with the context, that clause means additional rights of way and property of a tangible kind that may be acquired and added to the property and used in connection with it, as side tracks, stations, engines, &c.

Probably a lease of another road, which might be used in connection with the original mortgaged road, might be, as was held in one case, "after-acquired property;" but this is something new and added to the original.

But all the decisions on this question show, as we claim, that under this clause the moment the property is acquired the mortgage takes hold of it and becomes a lien on it. When it operates at all it requires no action by the mortgagee to make it take effect. No consent, adoption, or ratification is required.

This question is very well considered, and the authorities cited in 1 Jones on Mortgages, late third edition, sections 149 to 161.

This late edition of Jones' is much more full and complete on this question and on the question of the assumption of mortgage debts by the vendee than the former editions.

It must, however, be after-acquired property in this

case—something acquired since the making of the mortgage, which is an accession or addition to the main property, as side tracks, a branch road, lease of another road used in connection with the main road. As before said, this new property is brought under the mortgage as soon as acquired and subject to any claims or liens that may be upon it when acquired. In the beginning the mortgage covers the whole road. Carving out of the same thing a term for years is no addition to it; and if the term thus carved out were binding on the mortgagee it would, in many cases, totally destroy the value of the mortgage. It is only a part of the same thing which is already mortgaged.

The idea advanced by Judge Hoadley, on pages 46 and 47 of his brief, that the words of the mortgage, "franchises, privileges, and estate of the first party appertaining thereto, which the party of the first part now possesses or owns or may hereafter acquire," cover "all the legal rights which the lessor company then had" and all the personal contracts in regard to the property the mortgagor might see fit to make, is novel, but certainly unsupported by authority.

"Having exercised its franchise in granting a lease, and the right to grant the lease (that is, the franchise to grant the lease) having been mortgaged, the lease is mortgaged."

Is not this a play upon words? He uses the term franchise here as synonymous with power or right. It amounts to this, then, that whatever the mortgagor had the power or right to do may be mortgaged. It had the power to make a lease; therefore the lease when made is mortgaged. This will hardly do.

The franchise to be a corporation and the franchise of a corporation to run and maintain a railroad, collect fares, &c., are not the same, as is shown in the case of Coe *v.* Columbus R'y *et al.*, 10 O. S., 373.

Of course, the railroad property without the franchise or

power to run and operate the road would be of little value. The property and this franchise go together and are mortgaged.

But surely that gives no countenance to the idea that the mortgage reaches out and covers all the personal contracts the mortgagor may make concerning the road; nor to the idea that the mortgagee may hunt up these contracts, take a list of them, and adopt a part, such as he thinks good, and thus put them under the mortgage, and reject the others, and thus put them outside of the mortgage.

The mortgage is thus to cover contracts and choses in action, not according to its terms, but according to the whim or notion of the mortgagee. This would be a most uncertain, ambulatory, and shadowy thing indeed.

Certainly no such construction can be given to the contract in this case. The parties to it did not intend any such thing, and even if they did it can have no operation, because entirely contrary to the nature and purpose of a mortgage lien.

In St. Paul and Duluth R'y Co. *v.* United States, 112 U. S., 733, it was held that the mortgage did not cover or include a CONTRACT with the United States for carrying the mails. The terms of description in the mortgage were much more full and comprehensive than in this one now before the Court. The first proposition of the syllabus is: "1. A railroad mortgage conveying the road, franchises, and endowments does not cover or convey a contract with the United States for carrying the mails."

The opinion was delivered by Justice Mathews. The mortgagor had a valuable contract with the U. S. for carrying the mails. The St. Paul and Duluth R'y Co. claimed, as purchaser at judicial sale under the mortgage, to be the successor to all the rights of the mortgagor under the contract. In the opinion it is said: "The mortgage professes to convey the lands of the mortgagor, to which it was or might be entitled, * * * and its railroad, constructed or to be

constructed, right of way, and all tracks, bridges, viaducts, culverts, fences, depots, station-houses, and other similar houses, superstructions, erections, and fixtures held or to be acquired for the use of the railway or in connection therewith or the business thereof; also all locomotives, tenders, cars, rolling stock, or equipment, and all machinery, tools, implements, etc., and also all franchises connected with or relating to said railway and said line of telegraph, and all corporate franchises of any nature, including the franchise to be a corporation, and all endowments, income, and advantages, etc., to the above-mentioned lands, railroad, or property belonging or appertaining, and the income, rents, issues, and profits thereof."

Observe that this covers "franchises of any nature," "all endowments, income, and advantages," and "the income, rents, issues, and profits thereof." The court, in construing this clause, say: "We do not find in the mortgage or decree of sale any terms of description as to the property and interests conveyed sufficient to pass the interest therein of the original company to the purchasers at the sale. The same remark applies to the CONTRACT ITSELF. The appellant, by virtue of the sale of the railroad and property rights mortgaged, did not become assignee of the contract between the United States and the Lake Superior and Mississippi Railroad Co., and can claim nothing as such in this suit. There are no words of description in the mortgage which include it."

This case we think decisive against the plaintiff's claim in this behalf.

The parties to this lease, as we claim, ought to have rescinded it years ago, but having neglected to do so, the suit of Samuel Jeans *et al. v.* The P., C. & St. L. R'y Co. *et al.* was instituted in Jefferson county, Ohio, and by the decree of that court (see Record, page 27, E. J. Henry case) the lease was declared void and set aside November 24, 1885,

and the road, under said decree, surrendered back to the lessor company January 1, 1886.

That decree was entered by a court of competent jurisdiction, both of the subject-matter and of the parties, and we claim that it is conclusive as to this lease. THE LEASE IS DEAD. Moran cannot revive and enforce it. He has no lawful interest in it—never had. He was not, therefore, a necessary party to the suit in Jefferson county to set aside said lease.

The said decree, therefore, binds the whole world, and Moran with the rest. And we take it that that decree, under the circumstances before stated, is AN ABSOLUTE BAR to Moran's attempt in this Court to claim anything by virtue of the lease.

The proceeding in error in the supreme court of Ohio, by E. J. Henry *v.* The P., C. & St. L. R'y Co., Samuel Jeans, *et al.*, does not affect the matter.

The judgment setting aside the lease is still in full force. Execution only is stayed.

II.

THE LEASE WAS ILLEGAL.

The case ought to stop right here, so far as any claim is made by Moran to enforce this alleged lease; but on the merits, if the Court desires to hear further:

1st. We claim that the lease itself, as shown by the record and evidence, was illegal; that under the circumstances the directors of the P., C. & St. L. R'y Co. had no power or authority to divert the funds of that company to the payment of the debts of the Valley Company.

It may be said that this point is not clearly raised by the pleadings, but we claim that the point is properly before this Court in this equitable proceeding.

Moran, as mortgagee, is substantially asking this Court to

SPECIFICALLY ENFORCE this alleged contract of lease—to aid him in getting the funds of one company to pay the debts of another under pretense of this alleged lease. The chancellor will very properly desire to know whether this contract is legal and just and fair in all its parts. As a general rule, a court of equity will not aid in enforcing an illegal contract, a fraudulent one, or a hard and unconscionable one. Moran must come into a court of equity "with clean hands" and show a just claim upon its equity powers.

2 Story's Eq., sections 771 to 777.

On this point of the want of power of the Pan Handle Company to enter into this agreement to advance its funds to the other company we wish to call the attention of the Court especially to the very able and complete opinion of Justice Bradley in the case of the Pennsylvania R. R. Co. *et al. v.* St. Louis, Alton & Terre Haute R. R. Co.

118 U. S., 290 to 321.

The great point is that without statutory authority "it is a departure from the business of the corporation" to guarantee the debts of another company or loan its funds to another company.

The court cites and approves, among other authorities—

Pearce *v.* Madison and I. R'y Co., 21 Howard, U. S., 441.

Thomas *v.* West Jersey R'y Co., 101 U. S., 85.

Davis *v.* Old Colony R'y Co., 131 Mass., 275.

And this decision would seem to settle that question in this country, so far as judicial authority can settle anything.

Each corporation should be strictly confined to the limits of its own chartered business, and justice to the stockholders requires that the funds subscribed should be appropriated solely to its own legitimate business. The neglect to observe

this legal and moral principle—the corrupt and fraudulent management of many of our railroad corporations—has brought distrust and discredit upon the whole business. No man dare subscribe stock with the assurance that it will be honestly applied to the business for which it was subscribed. Such conduct is demoralizing and destructive to the best business interests of the country. The road may be first class, the business good and paying, but we are sure that the business will be so managed that the stockholder will get none of the benefits. If the enterprise is a failure, of course he gets nothing; but when it is a first-class success he is no better off and never will be until these rascally schemes are ferreted out and wiped out by the honest indignation of an independent judiciary.

In Coleman *v.* Eastern Counties R'y Co., 10 Beav., 1, Lord Langdale, among other things, said:

"If there is one thing more desirable than another after providing for the safety of all persons traveling on railroads, it is this: That the property of the railway companies shall be itself safe; that a railway investment shall not be considered a wild speculation, exposing those engaged in it to all sorts of risks, whether they intended it or not. Considering the vast property which is now invested in railways and how easily it is transferable, perhaps one of the best things that could happen would be that the investment should be of such a safe nature that prudent persons might, without improper hazard, invest their moneys in it. Quite sure I am that nothing of that kind can be approached if railway companies should be at liberty to pledge their funds in support of speculations not authorized by their legal powers and which might very possibly, to say the least, lead to extraordinary losses on the part of the railway company."

If the funds of one company are to be diverted "to support the speculations" of other companies, clear and plain statutory authority must be found granting the power.

Section 3300 of the Revised Statutes of Ohio confers the

power to lease a railroad not competing, but no fair construction of that section will show any authority to loan the funds of one company to another or to guarantee the debts of another.

"The power to lease and the power to guarantee are as divers as powers can well be. In the case of a lease by one railroad corporation to another corporation the lessee pays its own debt when it pays the rent, which it owes as rent and which it has agreed to pay as rent; in the case of a guarantee by the lessee of the bonds of the lessor company, should the guarantor be compelled to pay the bonds, principal or interest, or any part thereof, it pays an indebtedness of the lessor company, and consequently may compel a reimbursement thereof."

See Jones on Railroad Securities, section 351.

The power to aid in the "construction" of another company is very different from this.

It is true that under the power to lease, or rather under pretence of exercising that power, great wrongs may be perpetrated by agreeing to pay enormous sums by way of rent and in other sham ways; but the power to lease is given, the power to guarantee is not.

In the case before referred to (118 U. S., 290) Justice Miller says: "These companies might as well have assumed the power to loan them money or indorse their notes or any other transaction as to guarantee the performance of a void contract by one company to another."

Substance and not mere form must govern the transaction, and the power to guarantee cannot be exercised, indirectly, through the mere form of a lease.

In Morawetz on Private Corporations, sec. 423, it is said: "The corporate funds cannot be given away gratuitously. The property and funds of a corporation belong to its shareholders, and cannot be devoted to any use which is not in accordance with their chartered purpose, except by unanimous consent. No agent of the corporation has implied au-

thority to give away any portion of the corporate property or to create a corporate obligation gratuitously." * * * "Thus a railroad company is not liable upon a guaranty of the bonds of a connecting road made by its agents without a consideration and induced merely by the expectation of an increase of business."

Davis *v.* Old Colony R'y Co., 131 Mass., 258.
Pearce *v.* Madison and I. R'y Co., 21 Howard, 441.
7 Wisconsin, 59.

We submit that this clause for the "advance" is unauthorized and illegal, and the further misapplication of the funds of the Pan Handle under it should be stayed.

And, even if the contract were not illegal, we submit that, as between the parties, it would be unjust, inequitable, and unreasonable to require a further advance of the funds of one company to pay the debts of the other.

If there ever was any honest meaning in the clause for the "advance" the money was to be returned or repaid. The proof shows that this is impossible. The lessor is insolvent, can never repay, does not and cannot perform any of the covenants or stipulations of the lease on its part; and surely under well-settled principles of equity, this inability of the one party to perform or its neglect or refusal to perform the covenants and stipulations on its part renders it unjust and inequitable to further hold the other party; and Moran can have no better right than the lessor.

2 Parsons on Contracts, 565, 192.
3d vol. Pomeroy's Eq., sections 1405–1107.

It is a claim by Moran to wreck and ruin forever the minority stockholders of the Pan Handle Company through the machinery of this lease.

Over $1,000,000 of the funds of the one company have already gone into the pockets of the bondholders without

consideration, and the same is a total loss to the minority stockholders.

This wrong can now be corrected without injury to any innocent party—without injury to any one.

The circumstances which ought to control the judicial discretion of the chancellor, when asked to specifically enforce a contract, are briefly and well stated in note 3 to section 1405 of 3d vol. Pomeroy's Eq., as follows:

"If, then, the contract itself is unfair, one-sided, unjust, conconscionable, or affected by any other inequitable feature, or if its enforcement would be oppressive or hard on the defendant or would prevent his enjoyment of his own rights or would work any injustice, or if the plaintiff has obtained it by sharp and unscrupulous practices, by overreaching, by trickery, by taking undue advantage of his position, by non-disclosure of material facts, or by any other unconscientious means, then the specific performance will be refused."

We submit that every element of wrong and injustice above stated can be found in the plaintiff's unjust claim in this case.

III.

Neither the lessor nor Moran should be allowed TO FURTHER ENFORCE this alleged lease or contract because the means, powers, and influences by which it was in form brought about were a breach of trust and a fraud on the minority stockholders.

It is elementary law that the directors are trustees for all the stockholders, and holding this fiduciary relation they must act in entire good faith for the best interest of the stockholders.

Pierce on Railroads, 37.
Taylor *v.* Miami Ex. Co., 5 O., 162.
Goodin *v.* Cincinnati & W. Canal Co., 18 O. S., 169.
Rolling Stock Co. *v.* Railroad, 34 O. S., 450.
3 Pomeroy's Eq., section 1095.

Where there are common directors in both companies whose interests are adverse they are not in a condition to make a binding contract with one another, however fair or just it may appear to be in the special case.

Devou *v.* Fanning, 2 John's Ch., 252–268.
1 White & Tudor's Leading Eq. Cases, 257.
American & English Railroad Cases, vol. 13, page 102.
American & English Railroad Cases, vol. 15, page 1.
American & English Railroad Cases, vol. 16, page 461.
Morawetz on Corp., sections 522, 528, 529.
21 Kansas, 365.

These authorities, we think, conclusively establish that a contract brought about by such means and influences as shown in this case is voidable in equity at the option of the injured party.

In Goodin *v.* C. & W. Canal Co., 18 O. S., 183, WELCH, J., delivering the opinions of the court, severely, but not unjustly, characterizes such attempts to trample upon the rights of the minority. He says:

"To undertake, by getting control of the company and then, under pretence of acting as agents and trustees for all the stockholders and creditors, deliberately to trample under foot the rights of the minority is rather A SHARP PRACTICE and one which a court of equity will never tolerate. A director whose personal interests are adverse to those of the corporation has no right to be or act as a director As soon as he finds that he has personal interests which are in conflict with those of the company he ought to resign. No matter if a majority of the stockholders, as well as himself, have personal interests in conflict with the company. He does not represent them as persons or represent their personal interest. He represents them as stockholders and their interests as such. He is trustee for the company, and whenever he acts against its interests, no matter how much he thereby benefits foreign interests of the individual stock-

holders or how many of the individual stockholders act with him, he is guilty of a breach of trust, and a court of equity will set his acts aside at the instance of stockholders or creditors who are damnified thereby. Any act of the directory by which they intentionally diminish the value of the stock or property of the company is a breach of trust, for which any of the stockholders or creditors may justly complain, although all the other stockholders and creditors are benefited IN SOME OTHER WAY more than they are injured as such."

Judge Hoadly claims that the Pennsylvania Railroad Company, although a majority stockholder in both the lessor and lessee companies, and although it held a majority of the mortgage bonds of the Valley Company, and thus held large adverse interests to the stockholders in the Pan Handle Company, had, nevertheless, the right to vote its stock and use its controlling power to subserve its own interests, even if they were thus adverse to the interests of the stockholders of the Pan Handle Company.

This claim, we submit, is not at all supported by reason or authority. It has no right, under such circumstances, to despoil one corporation in order to build up the other, or to advance and benefit its own secret and adverse interests.

Of course, as a general rule, the majority stockholder has the right to control the corporation, and if he have no adverse interests to be subserved, he will be likely to act for the best interests of all. He is bound to fair dealing however.

In Meeker *et al. v.* The Winthrop Iron Company, reported in 9th vol. Cincinnati Law Bulletin, page 325, the late Judge Baxter, speaking of this power of control over both companies, among other things said:

"Does this resolution validate and make effectual a contract that would otherwise be declared void? The ownership of a majority of the capital stock of a corporation invests the holders thereof with many and valuable incidental rights. They may legally control the company's business,

prescribe its general policy, make themselves its agents, and take reasonable compensation for their services. But in thus assuming the control they also take upon themselves the correlative duty of diligence and good faith. They cannot lawfully manipulate the company's business in their own interest to the injury of other corporators. Any contract made by them in behalf of their principal with themselves or with another for their personal gain would be voidable at the option of the company."

That was a case where the one party controlled both corporations and had a lease of valuable property made substantially to himself. The lease was set aside. The court further remarking: "The law does not vest majority stockholders with any such dangerous power, invite such peculations, or open the door to such abuses."

And, further, as the Pennsylvania Railroad Company absolutely controlled both lessor and lessee, the contract was one of form MERELY, and of no binding force upon the MINORITY STOCKHOLDERS OF EITHER COMPANY. There was no real consent here, and, therefore, no contract.

The parties must be free to accept or refuse the terms offered. Substance and not form merely must control this matter. There was no substance in it. It was all a sham—mere form—forced upon unwilling parties. To hold such a thing a contract would make the law a vain thing indeed.

I think I may safely affirm that there is no well-considered decision of any respectable court sustaining a contract brought about in such a way as this, and surely no decision where a court of equity has undertaken to specifically enforce and help carry out such a contract.

That such shams will not be enforced against non-consenting minority stockholders is too clear for argument, and submission for a time to the wrong is no reason for a submission to future wrongs of a similar character.

In Morawetz on Corporations, sec. 263, it is laid down:

"A shareholder who has acquiesced in an authorized act is not bound to submit to all future acts of a similar character. Nor is a shareholder who has acquiesced in the making of an unauthorized and illegal contract necessarily precluded from applying to the court to restrain its performance. If a contract made on behalf of a corporation is unauthorized and void, it is the duty of the company to refuse to perform it. To proceed and perform the void agreement would be a further wrong, and might result in a misapplication of the company's funds and a forfeiture of its franchises."

And a ratification or condonation by stockholders when controlled by the SAME POWER that conceived the wrong does not help it. In 2 vol. Morawetz on Corporations, sec. 622, it is said:

"But the supreme court of Rhode Island said: 'To hold that a corporation could gratuitously condone or release such a fraud by anything short of unanimous consent would be in effect to hold that a president or director who can control A MAJORITY VOTE in the corporation may rob or despoil it with impunity.' A majority, in our opinion, could no more condone such a wrong gratuitously than it could originally have sanctioned it."

In 2 vol. Pomeroy's Equity, sec. 964, it is stated:

"Wherever a confirmation would itself be subject to the same objections and disabilities as the original act, a transaction cannot be confirmed and made binding, for confirmation assumes some positive, distinct action or language, which, taken together with the original transaction, amounts to a valid and binding agreement. * * * If the original undue influences remain, or if the act is simply a continuation of the former transaction, or if the party wrongfully supposes that the original contract or transaction is binding, or if he has not full knowledge of all the material facts and of his own rights no act of confirmation, however formal, is effectual; the avoidable nature of the transaction is unaltered."

The case in 34 O. S., 450, does not militate against the general weight of the authorities above cited. It is criticised and explained in the 15th vol. of the American and English Railroad Cases, page 1.

But even AT LAW it only holds that the "mere fact that A MINORITY of its board of directors are also directors of the other company" does not render the contract void or voidable.

But the evidence here shows that we have many more circumstances than that "mere fact"—as the want of consideration—the absolute control by the majority stockholder in both—the adverse and secret interest of the Pennsylvania Railroad Company in its ownership of the $752,000 bonds—and the fact that the president of the Valley Company, H. J. Jewett, was also general counsel for the Pan Handle and also for the Pennsylvania Railroad Company and was one of the main agents in getting up the lease.

IV.

Again, this is not the case of a wrongful contract FULLY EXECUTED. It is a CONTINUING CONTRACT, requiring daily and continuous acts in performance of it and in carrying it out, and, being illegal and unjust, the further execution of it should be stayed.

So far as it has been executed, and property acquired, and money expended under it, we may be without remedy to recover anything back, but a further misapplication of funds under it will be restrained.

Morawetz on Corporations, sections 691, 693, 707, 712.
Thomas *v.* West Jersey R'y, 101 U. S., 86.
Whitney Arms Co. *v.* Barlow, 63 N. Y., 62–68.
Hafer *v.* N. Y. & L. E. & W. R'y Co., 14 Law Bulletin, 68.

It was the duty of the company to rescind this agreement at the earliest moment, and, as said by Justice MILLER in

Thomas *v.* Railroad, *supra*, "the present case does not come within the principle that requires that contracts, which, though invalid for want of corporate power, have been fully executed, shall remain as the foundation of rights acquired by the transaction." The suit referred to was one to enforce a part of the agreement which had not been executed.

It was claimed by counsel in the case of The Pennsylvania Railroad Co. *v.* St. Louis, etc., R'y Co., 118 U. S., 290, before referred to, that the contract had been fully executed, and that, therefore, it was too late to make the defence of want of power or illegality; but Justice MILLER, in answer to the claim (there having been ten years performance under the contract complained of), said:

"Undoubtedly there are such decisions of courts of high authority, and there is such a principle, very sound in its application to appropriate cases; but we understand the rule in such cases to stand upon the broad ground that the contract itself is void, and that neither what has been done under it nor the action of the court can infuse any vitality into it. We know of no well-considered case where a corporation which is a party to a CONTINUING CONTRACT which it had no power to make seeks to retract and refuses to PROCEED FURTHER can be compelled to do so. As was said in Thomas *v.* Railroad (a case so often in point here), 'Having entered into the agreement, it was the duty of the company to rescind or abandon it at the earliest moment. * * * Though they delayed this for several years, it was nevertheless a rightful act when it was done.'"

Again, as to the point made that the contract had been executed and acquiesced in for a long time, Justice MILLER, near the close of his opinion in the above case, said:

"There is wanting in the case of the guaranteeing companies one of the strongest reasons usually urged in support of the estoppel, as it is sometimes called, namely, that the recalcitrant party HAS RECEIVED THE MONEY or the property of the other; for, so far from these guaranty companies having received from the plaintiff any money or property, they are the parties who have been PAYING MONEY and the plain-

tiff receiving it for rent of its road. They are not, therefore, estopped on any principles of that doctrine from ceasing to pay money on an illegal contract because they have hitherto done so. On the contrary, as we have already said, the duties of these directors to their stockholders is TO CEASE to PERFORM a contract to which they were never bound."

This is a most pertinent answer to Moran's claim to have this lease enforced and continued for his benefit.

The Pan Handle Company should have ceased long ago, it is true, to allow its funds to be taken to pay the debts of the other company.

And surely because this wrong has been suffered for years is no reason why it should be suffered forever, or for ninety-nine years, which will be the same as "forever" to most of us.

The past wrong can never be righted, but all future wrongs of this nature should be prevented.

V.

It is claimed that the minority stockholders are now estopped to object to the further execution of this contract by reason of their long delay, laches, or acquiescence.

This claim is wholly without foundation in this case.

The delay has not hurt Moran. It has been to the injury of nobody except these defendants.

Moran parted with nothing, invested nothing on the faith of this lease. He is injured in no way. His mortgage is still on the Valley road. That company is still entitled to the entire earnings and proceeds of its own road. The road is placed in better repair and better condition than ever before. If the entire proceeds of his own mortgaged property, thus placed in good condition, will not meet the interest on his mortgage, he has no just right to reach into the treasury

of the Pan Handle Company for the money with which to pay this old debt.

Some delay, however, was not only justified, but absolutely required in order to give the road a fair trial under this arrangement if it was to be carried out in good faith. The contract for this "advance" provides that the advance is to be repaid out of the future profits, and a fair trial was only reasonable and proper, under the circumstances, to ascertain whether there could be any return.

Delay, however, counts for nothing until the fraud or wrong is discovered.

These minority stockholders did not in fact know how the wrong was effected or what it was until the spring of 1885.

And even Robert Sherrard, who had been a director in the Pan Handle Company for many years, did not know of the adverse interest of the Pennsylvania Railroad Company in its holding these bonds. (See his testimony.)

But it is said they are presumed to have known that the officers of the company knew and that they are bound by the knowledge or notice of their agents. This is generally true. But, as the law is founded in reason, there is this very important exception to it:

Where the wrong-doers are the officers themselves or the wrong-doers have HOSTILE CONTROL of a majority of shares—in such cases mere notice to plaintiff or its directors is unimportant. The stockholders, in such case, are compelled to bring suit in a court of equity to have the wrong righted, and they cannot be TURNED OUT OF COURT on the technical ground that the officers of the company who committed the wrong knew of it, and that they are bound by what their own officers knew; and no demand upon the corporation in such case is necessary before the bringing the suit, for the demand would be a vain thing.

"It would be wholly contrary to establish principles of justice to permit the authors of a wrong to conduct a litiga-

tion against themselves as agents of the injured complainant."

Morawetz on Corp., secs. 242, 252.
Peabody *v.* Flint, 6 Allen, 52.
Pacific R. R. of Mo. *v.* Mo. Pacific R. R. Co., 111 U. S., 505.

In this last case, a case where the directors had hostile control and did the wrong, the court say:

"Under such circumstances mere knowledge by or notice to the plaintiff or its directors or officers or more or less of its stockholders is unimportant, and the plaintiff cannot be concluded by the failure of any number of its stockholders to do what unfaithful directors ought to have done, unless a case is shown of such acquiescence, assent, or ratification as would make it inequitable to permit what has been done to be set aside, or unless the rights of purchasers have subsequently intervened to an extent creating an equitable bar to the granting of relief. The bill in this case does not show such a state of things.

"While stockholders, more or less in number, may be allowed to interpose, if they have the means or the inclination to take upon themselves the burden of such gigantic controversies or are involved in the railroad transactions of the present day, it would go far to legalize condonation of such transactions as are set forth in this bill, if mere knowledge by helpless stockholders of the fraudulent acts of their directors were to prevent the corporation itself from seeking redress if it acts promptly when freed from the control of such directors."

2 Morawetz on Corporations, sec. 631*d*.

And, further, this delay or acquiescence must not only "be made with a full knowledge of the facts, but of the law; or, in other words, of the way in which the facts would be dealt with by a court of equity."

1 Equity Leading Cases (White & Tudor), page 259, and cases cited, and also page 236.

The rule is well stated in 2 vol. Pomeroy's Eq., sec. 817, as follows:

"The acquiescence must be with knowledge of the wrongful acts themselves and of their injurious consequences; it must be voluntary, not the result of accident nor of causes rendering it a physical, legal, or moral necessity, and it must last for an unreasonable length of time, so THAT IT WILL BE INEQUITABLE EVEN TO THE WRONG-DOER TO ENFORCE the peculiar remedies of equity against him. * * * What will amount to a sufficient acquiescence in any particular case must largely depend upon its own special circumstances."

2 Pomeroy's Eq., sec. 817.

The true rule is well stated in the case of The Rolling Stock Co. *v.* Railroad, 34 O. S., 462, thus:

"What constitutes a reasonable time must largely, if not wholly, depend upon the circumstances of the particular case. Where the consequences of delay are or may prove injurious to the other contracting party, especially where large expenditures, to the knowledge of the principal, are being made on the faith of the validity of the contract, the law requires prompt action on his part if he would avoid responsibility for the acts of the agents. His right to avoid being one, arising in equity, is governed by the rules upon which that court administers justice."

Rolling Stock Co. *v.* Railroad, 34 O. S., 462.
Piatt *et al. v.* Longsworth's Eq., 27 O. S., 199.
Paschall *v.* Hinderer, 28 O. S., 582.

"No injustice will be done to any innocent third party."

2 Pomeroy's Eq., sec. 965.

There was no standing by here in expectation of profits or benefits, if any should arise out of the contract; and, besides, the lessee could receive no profit in any event.

The circumstances of each case must determine its equities. There are no two cases precisely alike. No iron-clad rule governs.

But, surely, in this case there is no element of this kind

of estoppel—the delay has not proved injurious to the other contracting party. He made no investments or expenditures on the faith of it. In short, he is injured in no way by its rescission. He is not only left in *statu quo*, but in a much better condition than he was before, as before stated.

VI.

It is claimed that the Pan Handle Company is the real party that instituted the suit in Jefferson county to set aside this lease, and that that suit was collusive. This is not the fact. But, even if it were so, how can it benefit Moran?

The facts make it absolutely certain that the corporation never should have entered into such a contract. The corporation should use its own property for the benefit of its own stockholders. It should never have promised to "advance" any of its funds to pay the debts of another company. And, surely, the very moment, at least, that it was ascertained that this "advance" could not and would not be returned or repaid, the corporation should have taken action to prevent any further waste of its funds.

And in case it was not able or willing to do so, or was still under the control of the power that caused the original wrong, any stockholder might proceed in equity, by complying with the well-settled rules and conditions in such cases.

3 Pomeroy's Equity, sec. 1095.
Hawes *v.* Oakland, 14 Otto, 450.

The suit is maintained directly for the benefit of the corporation, the stockholder's interest being worked through the corporation.

And the suit is thus allowed to proceed "solely to prevent a failure of justice," as stated by Pomeroy in section 1095.

The Pan Handle management, if they have any desire to protect their own interests, must and ought to desire that

this lease be set aside, the wrong righted, and their stockholders protected.

But whether they have any such desire or not cannot affect the rights of these minority stockholders.

As said in the note to section 1095, in 3 vol. Pomeroy's Eq.:

"As a general rule, the company must sue in respect of a claim of this nature, but general rules have their exceptions, and one exception to the rule requiring the company to be plaintiff is that where a fraud is committed by persons who can command a majority of votes the minority can sue. The reason is plain, as, unless such an exception were allowed, it would be in the power of a majority to defraud the minority with impunity. In this case the defendant, Harris, holds such a number of shares that he can outvote those who wish the sale set aside. By reason, therefore, of his influence with the directors, and his number of votes, he has the SOLE CONTROL OF THE COMPANY."

These minority stockholders have been grossly injured and wronged, and they have a clear right to be protected, and if the present management of the Pan Handle Company will now not only not resist their attempt to obtain their rights, but will actively join in and assist them in protecting the corporate funds from further misapplication to the payment of the debts of the other company, it is not only their right, but their bounden duty to do so.

These minority stockholders have substantial interests of their own. They, in good faith, earnestly desire that this lease be set aside for the protection of their own proper interests. No one has lately purchased up stock for a song, for the purpose of bringing suit, but every one of them has held his stock for over 30 years and paid the full face value therefor. My own township of Cadiz paid for her stock, in cash, $100,000, and the rest of the townships and cities paid at the same rate.

The Pan Handle is a first-class through line, and for many

years has earned money sufficient to have paid some dividend upon the stock if it had been applied to its own proper purposes. These stockholders, as soon as informed of the iniquity by which these earnings have been for many years turned over to the bondholders of the Valley road, at once freely join and bring a suit for the protection of their rights. These rights they cannot obtain for themselves without, at the same time, benefiting the company and all the other stockholders. It is not, therefore, the Pan Handle's suit, although the corporation must be benefited by the relief which we ask, and unless the present managers are idiots or rogues they will not resist our claim to set aside the lease or attempt to reimpose this unjust burden upon the minority stockholders.

The statute of limitations is not applicable as a bar to these stockholders under the circumstances before stated, even if they were seeking affirmative relief, they having no knowledge of the constructive fraud or wrong, and the knowledge of the corporation or corporate authorities is not chargeable to them under the circumstances as before shown.

The general rule is well stated in 2 vol. Pomeroy's Eq., sec. 917, thus:

"No lapse of time, no delay in bringing a suit, however long, will defeat the remedy, provided the injured party was, during all this interval, ignorant of the fraud."

There are certainly no circumstances in this case of wrong to the other party to prevent the application of the rule. No innocent party has purchased bonds on the faith of this lease or had any right to do so.

Mr. McKee, who, in 1881, purchased $5,000 of the bonds, did not examine the lease at all, but saw fit, as he says, to take the loose statements of some persons made without any authority that the lease guaranteed the bonds.

See page 198 of complainant's testimony.